

Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, DC 20554

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FEDERAL COMMUNICATIONS COMMISSION  
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In the Matter of

Federal-State Joint Board on  
Universal Service

CC Docket No. 96-45

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**NYNEX REPLY COMMENTS**

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## SUMMARY

There is a general consensus that the Commission's definition of "core" universal service is consistent with the Telecommunications Act of 1996, and that this definition captures the services that are used by "a substantial majority of residential customers." The Commission should not include wireless technologies in the definition of universal service at this time, as wireless services are currently priced at a premium, and they are not used by most residential customers.

There is also wide agreement that the Commission must replace the current support mechanisms for small carriers and high cost areas -- the dial equipment minute ("DEM") weighting mechanism, long term support ("LTS"), and the existing universal service fund ("USF"). These mechanisms do not conform to the requirements of Section 254 of the Act, and they need to be replaced with a mechanism that is "explicit" and "equitable." Many parties agree with NYNEX that the Benchmark Cost Model ("BCM") should be used as a proxy model to calculate support for high cost areas. MCI is wrong in stating that the BCM "reflects the economic cost of the network." The BCM has several limitations that prevent it from approximating the actual cost of providing local telephone service. However, it is useful in identifying Census Block Groups that are relatively more costly to serve than other areas. Therefore, it can be used to target universal service support to high cost areas.

NYNEX disagrees with commenters who argue that the carrier common line ("CCL") charge is an implicit subsidy for universal service, and that the costs that are recovered through the CCL charge should be shifted to the end user common line ("EUCL") charge or that they should be recovered through the universal service fund. While the CCL charge may not reflect the way that common line costs are incurred, it does not support universal service as defined in the Act, and it does not belong in the fund. The Commission should allow the local exchange carriers ("LECs") to deal with the recovery of common line costs through pricing flexibility and access charge reform.

There is wide agreement that the Commission should use a surcharge on telecommunications revenues to fund universal service. NYNEX, and other commenters, support use of a surcharge on retail interstate revenues. This would make universal service funding explicit, and it would distribute the universal service obligation equitably among the carriers, as required by the Act. The Commission should not base the surcharge on total state and interstate telecommunications revenues, as that would be inconsistent with Section 254(d) of the Act. In addition, it would unduly burden the LECs' end user customers, who would pay both the federal surcharge, and possible state surcharges, on the same state revenues.

NYNEX received a positive public reaction to the NYNEX Education Plan ("NEP"), which is a specific mechanism for accomplishing a nationwide vision for bringing telecommunications services to the schools while giving state

education authorities and the schools themselves a great deal of flexibility in obtaining the services they really need. In response to comments that the NEP does not recognize the relatively higher costs that rural schools must incur to obtain telecommunications services, NYNEX has proposed a modification to the NEP that would create different Benchmark Prices and Discounts for rural and urban schools. In addition, NYNEX proposes a library assistance plan that would provide a similar funding mechanism for libraries.

The total cost for a narrowly targeted universal service fund, as proposed by NYNEX, would be \$2.9 billion for the first year. This would produce a 4.56% surcharge on interstate retail telecommunications revenues. Such a surcharge would be sufficient to achieve the purposes of the Act without unduly burdening rates for telecommunications services.

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In the Matter of

Federal-State Joint Board on  
Universal Service

CC Docket No. 96-45

**NYNEX REPLY COMMENTS**

The NYNEX Telephone Companies<sup>1</sup> ("NYNEX") hereby file their Reply to the Comments that were filed in response to the Commission's Notice of Proposed Rulemaking ("NPRM") in the above-referenced proceeding.<sup>2</sup>

**I. There Is A General Consensus That The Commission's Definition Of "Core" Universal Service Is Appropriate**

There is almost unanimous agreement with the Commission's definition of "core" universal service as a baseline definition.<sup>3</sup> Several commenters propose that the Commission include additional services in the definition of core

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<sup>1</sup> The NYNEX Telephone Companies are New York Telephone Company and New England Telephone and Telegraph Company.

<sup>2</sup> In the Matter of Federal-State Joint Board on Universal Service, Notice of Proposed Rulemaking and Order Establishing Joint Board, CC Docket No. 96-45, FCC 96-93, released March 8, 1996.

<sup>3</sup> See, e.g., MFS at p. 16; Teleport at p. 6; Bell Atlantic at p. 7; Frontier at p. 3; GTE at p. 5; Georgia PSC at p. 7.

universal service.<sup>4</sup> NYNEX's proposal to define core universal service as voice grade residential service with access to local and long distance calling, touch-tone dialing, directory listings, operator services, emergency services, and Telecommunications Relay Services ("TRS") would accommodate the interests of most commenters.<sup>5</sup> The Commission should require a carrier to provide these services as a single package, using its own facilities, or a combination of its own facilities and resale of another carrier's services, if it wishes to be designated as an eligible carrier to receive universal service fund support.<sup>6</sup>

Several commenters agree with NYNEX that core universal service should include only services using wireline technology.<sup>7</sup> Wireless services are not used by a substantial majority of residential customers,<sup>8</sup> they are sold at a premium price, and they are not substitutes for services that are provided over wireline technology. Entry into the local exchange market using wireless technologies is much easier than using wireline technologies, as wireless services do not require

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<sup>4</sup> See, e.g., AT&T at p. ii; LDDS WorldCom at pp. 7-8; MCI at p. ii; Sprint at p. 6; Time Warner at p. 4; US West at p. 7; USTA at p. ii; Alaska PSC at p. 13; California PUC at p. 6; New York DPS at p. 16; Illinois Commerce Commission at pp. 2-5.

<sup>5</sup> See, e.g., NYNEX at p. 11-12; AT&T at p. (ii); MCI at p. (ii); MFS at p.16; Sprint at p. 6; TCG at p. 6; USTA at p. (I); Colorado PUC at pp. 2-4; Florida PSC at pp. 5-7; Missouri PSC at pp.4-6.

<sup>6</sup> See AT&T at p. 21; Sprint at pp. 8-9; California PUC at p. 13; Florida PSC at p. 13; Missouri PSC at p. 9; Pennsylvania at p. 23. To the extent that an eligible carrier provided universal service through resale, the underlying carrier that provided the resold services should receive the universal service support funds.

<sup>7</sup> See, e.g., Georgia PSC at p. 7; NYNEX at pp. 12-13.

<sup>8</sup> See Section 254(c). Wireless services are subscribed to by only about 21% of the nation's households. See The New York Times, Section 4, Week in Review, The Great Unplugged Masses confront the Future, April 22, 1996.

massive up-front investments and maintenance of local loops.<sup>9</sup> Therefore, it is premature to include these services as part of the definition of core universal service.

## **II. The Current USF, DEM Weighting, and LTS Mechanisms Should Be Replaced Or Modified To Conform To The Telecommunications Act of 1996.**

### **A. The Commission Should Replace DEM Weighting With An Explicit Funding Mechanism And Eliminate Long Term Support.**

Several commenters agree with NYNEX that the current Dial Equipment Minute (“DEM”) weighting and Long Term Support (“LTS”) mechanisms need to be modified to conform to Section 254 of the Act.<sup>10</sup> DEM weighting shifts intrastate switching costs to the interstate jurisdiction for LECs who have fewer than 50,000 access lines in a study area.<sup>11</sup> LTS is a fund paid by LECs that are not NECA pool members to small LECs who are members of the pool.<sup>12</sup> Neither program satisfies the requirements of the Telecommunications Act of 1996 that support for universal service be “explicit” and that all telecommunications providers contribute on an “equitable and nondiscriminatory” basis.<sup>13</sup>

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<sup>9</sup> See A Policy Maker’s Guide to Deregulating Telecommunications Part 3: Solving the Local VS. long-distance Dilemma, By Adam D. Thierer; The Heritage Foundation February 21, 1993, p. 13.

<sup>10</sup> See, e.g., NECA at p. 7; GVNW at pp. 10-11; John Staurulakis at p. 7; Rural Telephone Coalition at p. 15; Bell Atlantic at p. 13.

<sup>11</sup> See Section 36.125

<sup>12</sup> See Sections 61.45, 69.4, 69.105, 69.603, and 69.502

<sup>13</sup> See 47 U.S.C. Sections 254(b)(5), 254(b)(4), and 254(e).



The LTS program does not support the definition of core universal service, as it is designed to help small LECs maintain lower carrier common line ("CCL") charges, which only affects rates for interexchange service. In addition, as is shown in the table below, LTS funding has grown by 22.5% over the last three years;

**LTS Payments**

(in millions)

Tariff Period	Industry Payments	NYNEX payments
94/95 period	\$364	\$42
95/96 period	\$403	\$46
96/97 period	\$446	\$51

This places an increasing burden on the large LECs, who charge higher CCL charges in order to provide a subsidy to smaller LECs. Therefore, LTS should be eliminated, and the NECA pooling LECs should recover these costs directly through their CCL charges.

DEM weighting does help keep down the cost of local telephone service, because it shifts local switching costs to the interstate jurisdiction, allowing small LECs to charge less for local exchange service (and to charge more for interstate local switching access services). The DEM weighting program should be restructured by removing the revenue requirements associated with it from the smaller LECs' interstate switched access rates, and by recovering those costs

through an explicit federal fund.<sup>14</sup> If DEM weighting were restructured at the same time that LTS was eliminated, the total switched access rates of the small LECs would increase by about \$171 million.<sup>15</sup>

**B. The Commission Should Adopt The Benchmark Cost Model To Support Universal Service In High Cost Areas.**

There is widespread support for using the Benchmark Cost Model ("BCM") to determine the level of subsidy required for price cap LECs to provide universal service to customers in high-cost, rural, and insular areas.<sup>16</sup> Since the BCM does not rely on a company's actual costs of providing service, it is both technologically and competitively neutral.<sup>17</sup> The BCM treats carriers equally, regardless of the size of the area served and regardless of whether they are incumbent LECs or new entrants.<sup>18</sup> In addition, the BCM allows for portability of the subsidy among eligible service providers.<sup>19</sup> As such, the model

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<sup>14</sup> With this support, the small LECs could avoid increasing their state rates when DEM weighting was discontinued.

<sup>15</sup> Elimination of LTS would cause the small LECs' CCL rates to increase by \$446 million, while elimination of DEM weighting would reduce their Local Switching rates by \$275 million, for a net increase of \$171 million. Elimination of DEM weighting would reduce the large LECs' interstate switched access rates by \$47 million. That amount could be recovered through a proxy model such as the Benchmark Cost Model, which includes switching costs.

<sup>16</sup> See AT&T at Appendix A, p. 1; LDDS WorldCom at p. 10; MCI at p. ii; Sprint at p. 8; TCG at p. 7; US West at p. 8; Florida PSC at pp. 9-10; Pennsylvania PUC at pp. 17-18; Wyoming PSC at p. 17.

<sup>17</sup> See Wyoming PSC at p. 7; Sprint at p. 11.

<sup>18</sup> See NYNEX at p. 10; Time Warner at p. 9.

<sup>19</sup> See Sprint at p. 12. See also Reply Comments of the NYNEX Telephone Companies, CC Docket 80-286, filed November 9, 1995.

should be used to calculate universal service support for price cap LECs providing "core" services to residential customers in high-cost areas.<sup>20</sup> To the extent that funding from the new universal service fund exceeded the old funding, that amount would be used by the receiving carrier to reduce some of the contribution that access and state toll rates provide to basic residential local service.

In terms of high-cost assistance for non-price cap LECs, NYNEX proposes no change to the status quo. Non-price cap LECs should receive high-cost assistance based on actual loop costs in their study areas, rather than using the BCM. The total 1995 high-cost assistance amount for non-price cap LECs is estimated to be \$401 million. These costs, together with the costs of DEM weighting, should be included in an explicit federal fund. While the Commission may want to adopt some of the modifications to the support mechanisms for small LECs that were advocated by other commenters, NYNEX's calculations assume that the Commission will maintain the status quo.

In its Notice of Proposed Rulemaking in CC Docket 96-98, the Commission invited comments on using the BCM as a proxy methodology for constraining the rates that States may set for interconnection and unbundled network elements under Section 251 of the Act.<sup>21</sup> Unlike MCI, NYNEX does not

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<sup>20</sup> See NYNEX at pp. 10-12.

<sup>21</sup> See In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, Notice of Proposed Rulemaking, CC Docket No. 96-98, FCC 96-182, released April 19, 1996, para. 137.

believe that the BCM "reflects the economic cost of the network."<sup>22</sup> The BCM was designed to identify discrete geographical areas where the cost of providing residential service is high relative to other areas. It is not valid as a ratemaking tool, and it should not be used for that purpose.<sup>23</sup>

First, the model does not include the costs of business lines. Even with regard to the cost of residential lines, the model makes assumptions regarding network architecture design and installation costs that cause it to seriously underestimate the actual cost in urban areas. For example, in urban areas with relatively short loop lengths, the model assumes copper distribution plant. However, due to restrictions on space in cable vaults and conduit in urban areas, the telephone companies have moved to the use of fiber facilities in their feeder plant in almost all cases. The model also seriously underestimates the cost of placing new facilities in those urban locations. Since the purpose of the model was to identify high cost rural areas, this underestimation of urban investment was not considered a problem given the model's intended use. However, any broad geographical summation of the BCM would yield investment totals that would be too low, a fact that all of the Joint Sponsors discussed and were aware of when they submitted the BCM to the Commission in Docket 80-286.

In addition, BCM understates the total cost of service, because it applies direct and indirect expense loading factors from the LECs' ARMIS reports,

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<sup>22</sup> MCI at p. 11.

<sup>23</sup> See Reply Comments of the NYNEX Telephone Companies, CC Docket 80-286, filed November 9, 1995, pp. 10-11.

dividing total expenses by total embedded investment. Applying those loading factors to a smaller investment base understates the expenses that would be incurred even if actual investment were reduced. For example, if the level of customer moves and inquiries requires a force of 1,000 people to staff the customer service centers, cutting the cost of loop and switch investment in half does not reduce the 1,000 customer representatives to a requirement of only 500. Similarly, applying current maintenance expenses per dollar of investment to lower switch investment amounts does not represent the actual costs of servicing such switches. As a result, the BCM understates expenses, even if all ARMIS direct and indirect loading factors are included. The understatement becomes more extreme if, as advocated by MCI, certain indirect expense factors are excluded.

Due to these limitations, using the BCM for ratemaking would be inappropriate, as it would produce cost estimates that are far too low. The model should be used only for its intended purpose -- to identify high-cost service areas that need universal service support.

**C. There Is No Need To Shift Large Amounts Of Access Revenues To The Universal Service Fund.**

Several commenters agree with NYNEX that the CCL charge is not a universal service subsidy, and that retaining the interstate CCL charge does not

violate the statutory ban on implicit subsidies.<sup>24</sup> However, others argued that the CCL charge is a subsidy element, because it recovers some of the fixed costs of an end user's local loop through a usage-based rate charged to interexchange carriers.<sup>25</sup> They argued that the CCL charge should be eliminated and that loop costs should be recovered entirely from the end user through an increase in the end user common line ("EUCL") charge.<sup>26</sup> This would increase the EUCL charge up to about \$7.00.<sup>27</sup> Some commenters have also argued that any common line costs that are not recovered through EUCL charges should be included in the Universal Service Fund.<sup>28</sup>

Section 254 of the Act does not require the Commission to eliminate or restructure the CCL charge, and it does not require an increase in local telephone rates to replace the CCL charge. As NYNEX demonstrated in its comments, the CCL charge does not support universal service.<sup>29</sup> The CCL charge is a pricing issue, which should be addressed as part of access charge reform and access pricing flexibility. In Docket 94-1, NYNEX proposed an Adaptive Regulatory

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<sup>24</sup> See Alaska PSC at p. 8; Bell Atlantic at p. 11; Florida PSC at pp. 21-22; Georgia PSC at pp. 11-13; Indiana Utility Regulation Commission at pp. 8-10; New York DPS at p. 8; Pennsylvania PUC at p. 23; Washington Utilities and Transportation Commission at pp. 18-20.

<sup>25</sup> See AT&T at p. 16; MFS at p. 2; Sprint at p. 20; Time Warner at p. 20; Ameritech at p. 21; BellSouth at p. 2; GTE at p. 15; Southwestern at p. (I); USTA at p. (ii); California at p. 20.

<sup>26</sup> Some State PUCs have argued that any effort to eliminate the CCL charge is likely to infringe upon the State's authority to advance universal service under Section 254(f) of the Act. See, e.g., Indiana Utility Regulation Commission at p. 8-10.

<sup>27</sup> See, e.g., AT&T at p. 16.

<sup>28</sup> See, e.g., BellSouth at p. 2.

<sup>29</sup> See NYNEX at pp. 3-8; see also Missouri PSC at pp. 20-21; New York DPS at p. 4.

Model that would match the level of LEC pricing flexibility to the level of local exchange competition. This model would allow the LECs to develop competitive rates for recovering common line costs and to avoid shifting costs to the universal service fund.

AT&T argues that the Commission should price all access services on the basis of total service long run incremental cost ("TSLRIC"), and that the universal service fund should only recover the shortfall for services that are priced below TSLRIC.<sup>30</sup> AT&T argues that this would eliminate "inefficiencies and supracompetitive profits." AT&T does not define TSLRIC, and it does not substantiate its claim that pricing above that level is inefficient or unreasonable. We note that the Commission is considering TSLRIC pricing proposals in Docket 96-68 for interconnection under Section 251 of the Act. To the extent that TSLRIC pricing of access services or interconnection were based on theoretical, forward looking investment and expenses, it could cause the LECs to recover revenues that were less than their actual costs of service. Any mandatory restructuring of access charges, based on TSLRIC or on any other basis, must address alternative means of cost recovery, such as through repricing (as proposed by NYNEX).

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<sup>30</sup> See AT&T at pp. 4-8.

### **III. Contributions To Universal Service Funding Should Be Based On Total Interstate Retail Revenues.**

There is wide agreement that contribution to universal service support should be based on some sort of surcharge on revenues.<sup>31</sup> The differences among the proposals primarily concern which measure of revenues to use for allocating universal service obligations among the industry participants -- total retail telecommunications revenues, interstate retail revenues, gross interstate revenues net of payments to other carriers subject to the funding requirement, etc. NYNEX, along with some other commenters, believes that including a surcharge on interstate retail revenues in end user customers' bills is the most competitively neutral and fairest method of assessment.<sup>32</sup> As the Wyoming PSC explained;

This method could explicitly identify subsidies by showing universal service fund charges and payments directly on customer bills. End users would thereby be informed of the costs of the system. The charges and credits could be clearly identified and equally shared among providers and end users. This will help competition to develop rationally in a more informed marketplace.<sup>33</sup>

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<sup>31</sup> See AT&T at p. 7; NYNEX at pp. 23-24; NECA at pp. 17-18; LDDS WorldCom at pp. 3-4; MCI at p. 12; MFS at pp. 23-24; Sprint at p. 4; Ameritech at p. 23; BellSouth at p. 15; Cincinnati Bell at p. 14-15; Southwestern Bell at p. (I); US West at p. 16; USTA at p. (ii); GVNW at p. 4; California PUC at p. 21; Colorado PUC at p. 6; Florida PSC at p. 25; Idaho PSC at p. 17; Maine PUC at p. 2; NECA at pp. 17-19; New York DPS at pp. 9-10; Wyoming PSC at pp. 4-5.

<sup>32</sup> See, e.g., Southwestern Bell at p. (I); USTA at p. (I); Wyoming PSC at pp. 4-5; GVNW at p. 4.

<sup>33</sup> Wyoming PSC at pp. 4-5



Making the assessment explicit and visible to the end users is very important, since it would reveal how universal service is being supported, and this would naturally improve accountability for federal universal service costs. Embedding universal service surcharges in the carriers' rates would create distortions in the marketplace, and there would be no direct accountability for universal service costs.

Some commenters propose assessing the universal service surcharge on total revenues instead of on interstate revenues.<sup>34</sup> This would be contrary to Section 254(d) of the Act, which contemplates that only interstate telecommunications carriers would contribute to the federal universal service fund. As the New York DPS noted;

We find no indication of congressional intent to change the existing jurisdictional configuration of federal and state authority and responsibility for interstate and intrastate services. Nor did Congress see fit to advance a new model that would significantly alter current interstate and intrastate universal service support mechanisms. Therefore, we do not expect the Commission to require carriers to contribute intrastate revenues to any interstate universal service funding mechanism, consistent with Section 152(b) of the Communications Act.<sup>35</sup>

In addition, if the surcharge were applied to state retail telecommunications revenues, it would unfairly shift most of the burden of funding interstate universal service cost recovery to local telephone rates, and it could adversely impact state methods of supporting universal service. For example, assume that a customer had a total monthly bill of \$40, broken down

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<sup>34</sup> See AT&T at p. 7; Sprint at p. 4, GTE at p. 17.

<sup>35</sup> New York DPS at p. 9; *see also* California PUC at p. 21.

into a bill for state local telephone service of \$30 and a bill for interstate long distance service of \$10. If the federal surcharge were applied to total telecommunications revenues, it would apply to \$40 and not just to the \$10 interstate portion of the bill. If the state applied a surcharge to the \$30 of state revenues, as permitted by Section 254(f) of the Act, the customer contribution to the total interstate and state universal service funds would be based not on the total monthly bill of \$40, but on an artificially inflated bill of \$70 (\$40 for the interstate fund and \$30 for the state fund). Under NYNEX's proposal, federal surcharges would only apply to the \$10 interstate portion of the end user's bill, and state surcharges would only apply to the \$30 state portion of the bill.

AT&T's assertion that a surcharge on both interstate and intrastate retail revenues "obviates altogether the potentially difficult problems associated with having to make jurisdictional determinations"<sup>36</sup> is completely misplaced. The TRS funding mechanism, which is based on interstate gross revenues, has been in place since July 23, 1993, and all carriers, including interexchange carriers, LECs, CLECs, mobile carriers and resellers, have been able to identify their interstate revenues without any problems. Similarly, the use of interstate retail revenues for the universal service fund should not cause any problems.<sup>37</sup> By applying the federal universal service surcharge only to interstate revenues, the

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<sup>36</sup> See AT&T at p. 9.

<sup>37</sup> While NYNEX proposes that the universal service fund exclude access revenues and reseller revenues, these minor differences from the TRS model would not make the surcharge any more difficult to administer.

Commission would preserve the authority of the states to fund state universal service objectives through a separate surcharge on state telecommunications revenues.

TCG's recommendation that "the Commission adopt a threshold market share of at least 1% of interstate net transmission revenue before a carrier is required to contribute to universal service funding"<sup>38</sup> would unfairly exempt many CLEC customers from any contribution towards universal service funding. The 1995 interstate retail revenues of the telecommunications industry is estimated to be around \$64 billion.<sup>39</sup> 1% of these revenues is \$640 million. There is no reason why a carrier with as much as \$640 million in total interstate retail revenues should be exempted from contributing towards universal service.

#### **IV. Support For Services To Schools And Libraries Should Be Both Sufficient And Flexible.**

In its initial comments, NYNEX proposed the NYNEX Education Plan ("NEP") to provide support to schools under Section 254(h) of the Act. The hallmark of this plan is its flexibility -- it would allow the Commission to establish the overall vision and funding mechanism, while reserving to State education authorities and the schools themselves the ability to choose how to apply support to obtain the services that the schools need. The comments from

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<sup>38</sup> TCG at pp. 13-14; See also MFS at p. 16.

<sup>39</sup> See Exhibit 1. The gross interstate revenues are \$86.4 billion; See *In the Matter of Telecommunications Relay Services, and the Americans with Disabilities Act of 1990*; CC Docket No. 90-571, released December 14, 1995.

the educational community show that schools need a variety of telecommunications services, including high-speed, broadband facilities, access to the Internet, wireline and wireless data transmission, advanced services, ISDN, digital satellite, video teleconferencing, interactive multimedia, and a host of other services and capabilities.<sup>40</sup> This confirms NYNEX's belief that the Commission should not select a specific set of services or capabilities that must be provided to each school, and that the states and the schools need the flexibility to purchase a broad array of services at a subsidized discount. The NEP would accomplish this by establishing a Benchmark Discount and a Benchmark level of funding per student that schools could apply to purchase any telecommunications services they need.

NYNEX received very positive reactions to the NEP when we presented it the open meeting of the Joint Board on April 12, 1996. However, some parties later expressed concern that the plan did not go far enough in recognizing the disparity in communications costs between urban and rural areas. Schools in rural areas generally face greater costs for telecommunications services due to the distances between educational institutions and due to the distances from Internet providers and other information service providers. Dedicated transport facilities are frequently much more expensive in rural areas than in urban areas, and dial-up calls to Internet and information service providers more often

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<sup>40</sup> See, e.g., U.S. Distance Learning Assoc. at pp. 6-11; New York State Education Department at p. 10; National School Boards Association at p. 14; Illinois Board of Education at pp. 6-7.

involve toll calls. Although the NEP would allow state educational administrators to vary the discount by school, based on factors such as income and need, the plan does not include an explicit urban/rural differential.

For this reason, NYNEX proposes that the NEP include disaggregated Benchmark Prices and Discounts for urban and rural areas. The Commission should gather data on the difference in costs between urban and rural areas of acquiring similar telecommunications capabilities. Based on these data, the Commission could vary the discount. For instance, suppose the Benchmark Price per-student to achieve a nationwide educational vision for access to telecommunications services was \$100, and that the Commission determined that a Benchmark Discount of 50% would be sufficient to achieve that vision. This would mean that the net price, per student, after the discount would be \$50. Suppose also that the \$100 Benchmark Price, which was an average for all schools, represented a \$75 Benchmark Price for urban schools and a \$200 Benchmark Price for rural schools. If the Benchmark Discount were 50%, the urban schools would pay \$37.50 per student, and the rural schools would pay \$100. However, if the Commission disaggregated the Benchmark Discount into a 33% discount for urban schools and a 75% discount for rural schools, both would pay a net price of \$50 (a 33% discount from \$75 for urban schools, and a 75% discount from \$200 for rural schools). Thus, the Commission could ensure that both types of schools could obtain telecommunications services at the targeted price.

Some commenters propose that the schools receive 100% discounts -- in other words, free service.<sup>41</sup> This would take into account the fact that telecommunications services are a small part of the total package of services, equipment, training and support that schools need to obtain access to information access. However, free telecommunications services would encourage schools to order services that might exceed their needs, and that might never be used. In addition, the Act contemplates a discount, not free service. Therefore, the Commission should specify a discount that would be sufficient to achieve the educational vision, without encouraging wasteful ordering of facilities.

NYNEX does not support proposals that telecommunications carriers be required to provide services to schools and libraries priced at incremental cost, and that they should be provided universal service funds only for discounts from the incremental prices.<sup>42</sup> Under Section 254(h)(1)(B), telecommunications carriers are entitled to compensation, either through the universal service fund or through offsets to the carriers' universal service obligations, for any discounts that they provide to schools and libraries if the amounts of the discounts have been approved by the Commission and the States and if the services are within the Commission's definition of universal service. If the Commission required

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<sup>41</sup> See, e.g., National School Boards Association at p. 11.

<sup>42</sup> See, e.g., American Library Association at p. 14; Illinois Board of Education at pp. 8-9; Sailor, A Maryland Library Project at p. 18.

unfunded discounts, it would establish the type of implicit subsidy that the Act specifically prohibits.

The NEP could easily be adapted to provide support for libraries. In Exhibit 2, NYNEX describes an assistance plan for libraries based on the “lab model” in the KickStart Initiative developed by the U.S. Advisory Council on the National Information Infrastructure. This plan would connect libraries to the information superhighway at a cost of approximately \$82.5 million in the first year for universal service funding of telecommunication services and inside wiring. The Commission should incorporate these estimates in the universal service fund, and it should use a model similar to the NEP, with Benchmark Prices, Benchmark Discounts, and recognition of urban/rural differentials.

## **V. NYNEX's Proposals For Universal Service Funding Would Not Unduly Burden Telecommunications Rates.**

If the Commission adopted a narrowly targeted universal service fund, as proposed by NYNEX, the resulting surcharge on retail interstate telecommunications rates would not be excessive. In the chart below, NYNEX shows the total funding that would be included in the new universal service fund. It would replace the current funding for Lifeline, Linkup America, USF, and DEM weighting, and it would include additional support for schools and libraries.

# NEW UNIVERSAL SERVICE FUND

(in millions)

	Category	Amount (millions)
1	Lifeline	\$123
2	Linkup America	\$19
3	High-Cost for Rate of Return Carriers	\$401
4	DEM weighting for Rate of Return LECs	\$275
5	High-Cost for price cap carriers based on BCM	\$520
6	Schools	\$1,445
7	Public Libraries	\$83
8	Health Care Providers	NA
9	Total (sum of Line 1 through Line 8)	\$2,866
10	Base Case Industry Interstate Retail Revenues	\$64,205
11	Adjusted Interstate Retail Revenues <sup>43</sup> (Line 10 - sum (Line 1 through Line 5))	\$62,867
12	Federal Surcharge (Line 9 / Line 11) <sup>44</sup>	4.56%

This would provide a sufficient level of funding to meet the objectives of the Telecommunications Act of 1996, and it would produce a reasonable surcharge that would not unreasonably burden the efficient pricing of telecommunications services.

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<sup>43</sup> On line 11, base case retail revenues are reduced by the sum of lines 1 through 5, since those amounts would be recovered through the universal service surcharge, rather than through the carriers' retail rates. Price cap LECs currently receive \$325 million of funding from the USF. The NYNEX proposal assumes that any additional funding that exceeded the old funding would be reflected in a reduction in interstate rates. Retail revenues are not adjusted for funding of schools and libraries, since these are new funds that are not currently included in the carriers' retail rates.

<sup>44</sup> This surcharge is based on the assumption that funding for schools and libraries is introduced in 1997; after the initial five year period, the ongoing cost for schools is assumed to be at a level of \$720 million, and for libraries at a level of \$78 million. At that point, the surcharge would drop to 3.40%. See Exhibit 1.



## VI. Conclusion

The record in this proceeding provides a basis for adopting explicit funding mechanisms that would support universal service as defined in the Telecommunications Act of 1996. Such mechanisms, if properly targeted, would not create a fund that was so large as to impede competition or the efficient pricing of telecommunications services.

Respectfully submitted,

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